

## Message Text

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APPROVED BY EB - MR. KATZ

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E.O. 11652: XGDS - 1

TAGS: ENRG, CA, US

SUBJECT: CANADIAN OIL EXPORTS

1. CANADIANS PROVIDED DEPARTMENT WITH COPY FINAL DRAFT OF NEW NEB REPORT ON OIL SUPPLY/DEMAND ON CONFIDENTIAL BASIS. REPORT WILL NOT BE RELEASED TO PUBLIC UNTIL NOVEMBER 5, AND WE WERE ASKED TO RESPECT CONFIDENTIALITY OF REPORT UNTIL THAT DATE. NEW EMR MINISTER GILLESPIE PLANS VISIT WASHINGTON THAT DATE AND IS REQUESTING MEETINGS WITH CHUCK ROBINSON, FRANK ZARB, ROGERS MORTON AND NEW INTERIOR SECRETARY KLEPPE.

2. NEB REPORT INDICATES FURTHER SIGNIFICANT DETERIORATION IN CANADIAN OIL SUPPLY PROSPECTS, REDUCING PERIOD OF PROTECTION FOR CANADIAN DEMAND TO FIVE YEARS (FROM 7.3 YEARS ESTIMATED IN NEB'S OCTOBER 1974 REPORT). AS A RESULT, NEB

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RECOMMENDS SUBSTANTIAL SHORTENING OF SCHEDULE FOR PHASE-OUT

OF OIL EXPORTS TO THE U.S., TERMINATING EXPORTS IN 1981 RATHER THAN 1983. ALLOWABLE EXPORTS IN 1976, WHICH WERE PROJECTED AT LEVEL OF 560,000 B/D IN 1974 NEB REPORT, WOULD BE LIMITED TO AVERAGE OF 460,000 B/D -- 510,000 B/D DURING FIRST SIX MONTHS, DROPPING TO 385,000 B/D IN SECOND HALF OF YEAR OR WHEN NEW SARNIA-MONTREAL PIPELINE GOES INTO OPERATION. SPECIFIC EXPORT VOLUMES FOR 1977 AND BEYOND ARE NOT

GIVEN, ALTHOUGH OUR ROUGH ESTIMATES BASED ON NEB CHART INDICATE FURTHER SHARP DROP TO 250,000 B/D IN 1977.

3. ON THE BASIS OF ANALYSIS UNDERTAKEN EARLIER THIS YEAR IN CONNECTION WITH JOINT WORKING GROUP ON OIL EXCHANGES, WE ESTIMATE THAT CANADIAN-DEPENDENT REFINERIES IN NORTHERN TIER STATES WITH NO ALTERNATIVE SUPPLY POSSIBILITIES IN OFFING REQUIRE MINIMUM OF SOME 250,000 B/D OF CANADIAN OIL. THE COMPRESSION OF THE PHASE-OUT SCHEDULE TO 1981, PLUS THE ABSENCE OF PRECISE INFORMATION ON ALLOWABLE EXPORTS AFTER 1976, IS LIKELY TO MEAN THAT CURTAILMENT OF CANADIAN EXPORTS WILL BEGIN TO CAUSE SUPPLY PROBLEMS EARLIER THAN ANTICIPATED. THE CANADIAN REQUIREMENT THAT 22.6 PERCENT OF EXPORTS BE RESERVED FOR PUGET SOUND REFINERIES IN PAD V COULD CAUSE SUPPLY PROBLEMS TO ARISE AS EARLY AS SECOND HALF OF 1976 UNDER NEB'S RECOMMENDED EXPORT LEVELS.

4. REQUEST YOU SEEK APPOINTMENT WITH GILLESPIE AS SOON AS POSSIBLE AND MAKE FOLLOWING POINTS:

-- WE APPRECIATE RECEIVING ADVANCE COPY OF DRAFT NEB OIL SUPPLY STUDY.

-- HOWEVER, WE ARE SERIOUSLY CONCERNED AT THE IMPACT THE NEB'S RECOMMENDED EXPORT LEVELS WILL HAVE ON REFINERIES DEPENDENT ON CANADIAN IMPORTS, PARTICULARLY IN NORTHERN TIER STATES, WHERE THERE ARE NO ALTERNATIVE SUPPLY POSSIBILITIES.

-- WE UNDERSTAND THE CANADIAN SUPPLY SITUATION AND THE POLITICAL REQUIREMENT TO ENSURE ADEQUATE PROTECTION FOR  
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CANADIAN DOMESTIC DEMAND.

-- HOWEVER, WHEN THE CANADIAN GOVERNMENT ANNOUNCED THE SCHEDULE FOR PHASING OUT OIL EXPORTS TO THE U.S. LAST NOVEMBER, THERE WAS A CLEAR COMMITMENT BY CANADA TO PROVIDE REFINERIES IN THE U.S., WHICH ARE DEPENDENT ON CANADIAN OIL SUPPLIES, WITH A REASONABLE PERIOD TO ADJUST TO THE CHANGE IN CIRCUMSTANCES.

-- THE NEW NEB REPORT RECOMMENDS A SHARP REDUCTION, 100,000 B/D, IN OIL SUPPLIES IN 1976 AND PROVIDES NO CLEAR INDICATION OF WHAT LEVEL OF EXPORTS WILL BE ALLOWED AFTER THAT.

-- IT IS CLEAR THAT ONE SIGNIFICANT CAUSE OF THE DETERIORATION IN CANADA'S SUPPLY POSITION STEMS FROM THE PROJECTED

DECLINE IN PRODUCIBILITY. THE NEB FOUND THAT THIS WAS DUE TO THE FAILURE OF EXISTING OIL RESERVES TO PERFORM AS WELL AS PREDICTED, BUT ALSO BECAUSE OF THE LACK OF ADEQUATE ECONOMIC INCENTIVE AND LACK OF CONFIDENCE IN THE CANADIAN INVESTMENT CLIMATE WHICH WERE ADVERSELY AFFECTING OIL EXPLORATION AND DEVELOPMENT.

-- THE SECOND PART OF THE PROBLEM, AND ONE DIRECTLY RELATED TO THE ALLOWABLE LEVEL OF EXPORTS, IS THE NEED TO PROVIDE FOR SUFFICIENT PRODUCTION TO SUPPLY THE SARNIA-MONTREAL PIPELINE NOW UNDER CONSTRUCTION.

-- IN VIEW OF THE CONTINUING DETERIORATION IN CANADA'S SUPPLY POSITION, WE WONDER WHETHER A WEST TO EAST OIL PIPELINE WILL BE ECONOMICALLY FEASIBLE. WE UNDERSTAND THE SARNIA-MONTREAL LINE IS BEING BUILT SO THAT IT CAN BE REVERSED WHEN IT BECOMES NECESSARY TO USE IT FOR TRANSPORTING IMPORTED OIL TO REFINERIES IN TORONTO AREA. IT APPEARS TO US, ON THE BASIS OF LATEST NEB REPORT, THAT REVERSAL OF THIS LINE WILL BE REQUIRED MUCH SOONER THAN ORIGINALLY ANTICIPATED.

-- THE SARNIA-MONTREAL PIPELINE WILL THUS BE OF ONLY LIMITED UTILITY IN IMPROVING CANADIAN ENERGY SECURITY.

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ADDITIONALLY, THE SHARP REDUCTION IN 1976 EXPORTS -- PARTICULARLY IN SECOND HALF OF YEAR -- AND THE COMPRESSION OF THE TIMETABLE FOR THE PHASE OUT WILL CAUSE SEVERE DISLOCATIONS FOR CANADIAN DEPENDENT U.S. REFINERIES.

-- WE PROPOSE CANADA DELAY USE OF THE NEW PIPELINE FOR MOVING DOMESTICALLY PRODUCED OIL EASTWARD. THIS WOULD PERMIT MAINTENANCE OF EXPORTS NEAR PREVIOUSLY SCHEDULED LEVELS AND PROVIDE U.S. REFINERS WITH VITALLY NEEDED TIME TO MAKE ARRANGEMENTS FOR ALTERNATIVE SUPPLIES.

5. YOU SHOULD INFORM GILLESPIE THAT OUR JOINT EFFORTS TO ENCOURAGE OIL EXCHANGE ARRANGEMENTS ARE ONLY NOW BEGINNING TO GENERATE INTEREST AMONGEST U.S. AND CANADIAN REFINERS. WE WILL SEEK TO PRESS REFINERS ON OUR SIDE

TO STEP UP THEIR EFFORTS TO WORK OUT SUCH SWITCHING  
ARRANGEMENTS, BUT THESE WILL OBVIOUSLY REQUIRE TIME.  
NEW EXPORT PHASE-OUT SCHEDULE WOULD ENSURE THAT REFINERS  
RECOGNIZE URGENCY OF THEIR TAKING PROMPT ACTION. HOWEVER,  
MORE TIME WILL BE NEEDED THAN NEW SCHEDULE PROVIDES.

6. WE WOULD APPRECIATE GILLESPIE'S COMMENTS ON OUR  
PROPOSAL. WE WOULD HOPE WE COULD WORK OUT SOME MUTUALLY  
ACCEPTABLE ARRANGEMENT BY THE DATE OF HIS PROPOSED VISIT  
TO WASHINGTON ON NOVEMBER 5. KISSINGER

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